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Foreign Investment and Measures Adopted on Grounds of Necessity: Towards a Common Understanding

by T. Gazzini

FOREIGN INVESTMENT AND MEASURES ADOPTED ON GROUNDS OF NECESSITY: TOWARDS A COMMON UNDERSTANDING

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I. Introduction

During the grave economic crisis that hit Argentina between 1999 and 2001, the Argentine government adopted a series of drastic measures which adversely and substantially affected *inter alia* foreign investment [1]. These measures generated a stream of claims by foreign investors concerning alleged violations of obligations stemming from bilateral investment treaties (BITs).

In five of them, decided by arbitral tribunals established under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention), United States investors argued that these measures were inconsistent with the BIT concluded between Argentina and the United States. Argentina denied any breach of the treaty and, in the alternative, defended the measures on grounds of necessity under both Article XI of the BIT and customary international law [2]. One award has been the object of a decision on annulment [3] whereas annulment proceedings are pending in all four other cases.

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[1] These measures included: (a) bank deposit freeze (Decree 1570, 1 December 2001) and limitation of withdrawal to 250 pesos/US dollars per week; (b) prohibition on transferring funds abroad (Decree 1570, 1 December 2001); (c) termination of peso convertibility (Emergency law 25,561, 6 January 2002 and Decree 260/02); (d) reschedule of term deposit and reduction of interest rates (resolution 6, 9 January 2002); (e) pesification of the US dollar (Decree 214, 3 February 2002; Decree 471, 8 March 2002 and Decree 644, 18 April 2002); (f) default and rescheduling of State financial instruments (Resolution 73, 18 April 2002).

[2] *CMS Gas Transmission Company* v. *Argentina*, ICSID ARB/01/8, Award, 12 May 2005; *LG&E Energy Corp., LG&E Capital Corp., LG&E International Inc*. v. *Argentina*, ICSID ARB/02/1, Decision on Liability, 3 October 2006; *Enron Corporation and Ponderosa Assets, L.P.* v. *Argentina*, ICSID ARB/01/3, Award, 22 May

These disputes have led to significantly different outcomes and raised concern about the coherence and legitimacy of the system of settlement of investment disputes [4]. The paper discusses how ICSID tribunals have dealt with these necessity pleas with a view to identifying common patterns and divergences on the main substantive and procedural issues. It focuses first on the legal nature of Article XI and Article 25 of the Draft Articles on State Responsibility prepared by the United Nations International Law Commission (hereinafter Draft Article 25) as expression of customary international law, as well as their co-ordination. It also briefly discusses the alleged self-judging character of Article XI and then examines and compares the conditions that need to be satisfied in order to adopt measures on grounds of necessity under Article XI and customary international law.

II. Outcomes of ICSID case-law

In *CMS*, the necessity plea was rejected and Argentina could not escape responsibility for certain breaches of the BIT caused by the measures adopted during the economic and financial crisis. Claimant was therefore accorded compensation for about 133 million dollars. The award almost entirely survived the annulment proceedings, although the *ad hoc* Committee expressed, within the limits allowed by Article 52 ICSID Convention, sharp criticism on a number of issues, including necessity. The *Enron* and *Sempra* Tribunals, which were chaired by the same president, substantially followed *CMS* and accorded to the Claimants, respectively, about 109 and 128 million dollars compensation.

In *LG&E*, the Tribunal accepted that between 1 December 2001 and 26 April 2003 the grave economic and social situation existing in Argentina allowed the adoption of the measures under discussion on grounds of necessity. It further held that certain

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2007; *Sempra Energy International* v. *Argentina*, ICSID ARB/02/16, Award, 28 September 2007; *Continental Casualty Company v. Argentine Republic*, ICSID ARB/03/9, Award, 5 September 2008. All decisions are available at http://icsid.worldbank.org/ICSID/Index.jsp and http://ita.law.uvic.ca. For the sake of simplicity, the cases are referred to throughout the paper by the name of the applicant.

[3] *CMS*, Annulment Decision, 25 September 2007.

[4] See, in particular, A. Reinisch, 'Necessity in International Arbitration. An Unnecessary Split of Opinions in Recent ICSID Cases? Comments on *CMS* v. *Argentina* and *LG&E* v. *Argentina* , 8 *Journ. World Inv. & Trade* (2007) 191; T. Christakis, 'Quel remède à l'éclatement de la jurisprudence CIRDI sur les investissement en Argentine? La décision du comité *ad hoc* dans l'affaire *CMS* c. *Argentine*', 111 *RGDIP* (2007) 879; W. Burke-White, A. von Staden, 'Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties', 48 *Virginia Jour. Int.l Law* (2008) 307; T. Gazzini, 'Necessity in International Investment Law: Some Critical Remarks on *CMS* v *Argentina*', 28 *Journ. Energy & Natural Resources Law* (2008) 450; J. Alvarez, K. Khamsi, The Argentina Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime', *International Law and Justice Working Papers*, 2008/5, NY University School of Law.

measures adopted by Argentina outside this period were inconsistent with the BIT and triggered responsibility on the part of Argentina. Compensation amounted to about 57 million dollars.

In *Continental*, the Tribunal held that the adoption of all measures before it, apart from those concerning the Treasury Bills (LETEs, for which compensation was fixed at about 3 million dollars), were justified on grounds of necessity and therefore entirely compatible with Argentina international obligations.

The diverging decisions hardly come as a surprise considering that these disputes call for a series of delicate assessments concerning, most prominently, the existence of a crisis serious enough to trigger the adoption of measures on grounds of necessity, the role of the host State in the management of the crisis, and the availability of alternative measures consistent with of less disruptive of the host State international commitments.

However unsatisfactory, the inconsistent outcome of these cases may be considered as an unavoidable side-effect of investment arbitration as "each tribunal remains sovereign and may retain, as it is confirmed by ICSID practice, a different solution for resolving the same problem" [5]. The crux of the matter remains whether the different outcomes were due to different assessment of the facts or to different interpretation and application of the relevant rules.

III. Legal nature of Draft Article 25 as expression of customary international law

The defence strategy of Argentina was based firstly on the rejection of the claim that the measures adopted during the crisis were inconsistent with the obligations owed to foreign investors. In the alternative, Argentina argued that these measures were adopted on grounds of necessity under Article XI BIT and under customary international law as codified in Draft Article 25.

Before assessing the necessity pleas, it is appropriate to discuss the legal nature of Article XI and Draft Article 25, as well as their co-ordination. It may be convenient to start with Draft Article 25 as its legal nature was relatively uncontroversial in the awards of the five tribunals and the decision of the *ad hoc* Committee. Draft Article 25 reads:

> 1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act: (a) Is the only way for the State to safeguard an essential interest against a grave and imminent peril; and (b) Does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

[5] *AES Corp*. v. *Argentina*, ICSID ARB/02/17, Decision on Jurisdiction, 26 April 2005, paras 30-31.

2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

(a) The international obligation in question excludes the possibility of invoking necessity; or

(b) The State has contributed to the situation of necessity [6].

In none of the cases referred to above, the Claimant challenged in principle the applicability of Draft Article 25 in investment disputes. Accordingly the different Tribunals did not elaborate on the issue but merely accepted that the Respondent could invoke Draft Article 25.

It is nonetheless worth noting that a tribunal established under UNCITRAL rules to settle a dispute between a British investor and Argentina held that Draft Article 25 being related exclusively to obligations between sovereign States is of little assistance in investment disputes [7]. This view is not convincing. The invocation by the host State of necessity under customary international law to justify a conduct otherwise contrary to its obligations under the BIT is precluded neither by the fact that foreign investors are the primary beneficiaries of the treaty, nor by the hybrid nature of international investment arbitration [8]. Regardless to the question whether the BIT imposes upon the host State a substantive obligation or a procedural obligation vis-à-vis foreign investors, an investment dispute opposes the former and the latter over alleged violations of treaty obligations. Since the source of the obligations allegedly breached is clearly an international one, it seems consequential to admit that the host State may invoke necessity under customary international law as a circumstance precluding wrongfulness. The real problem is then the co-ordination between

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[6] *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, UN Doc. A/56/10 (2001); J. Crawford, *The International Law Commission's Articles on State Responsibility. Introduction, Text and Commentaries* (Cambridge: Cambridge University Press, 2002). Also available at http://untreaty.un.org/ilc/texts/instruments/english/draft%20articles/9_6_2001.pdf. On the correspondence between Draft Article 25 and customary international law, see *CMS*, Award, para 315; Annulment Decision, para 121; *LG&E*, para 245; *Enron*, para 303; *Sempra*, para 344; and, in caution terms, *Continental*, para 238. See also *National Grid plc v Argentina*, UNCITRAL, Award, 3 November 2008, para 256. That Draft Article 25 (at the time Draft Article 33) reflects customary international law has been confirmed by the ICJ in *Gabcíkovo - Nagymaros Project*, Judgment, *I.C.J. Reports 1997*, p. 7, para 51-2.

[7] *BG Group Plc.* v *Argentina*, UNCITRAL, Award, 24 December 2007, paras 407 ff. The Tribunal nonetheless found that even assuming the applicability of Draft Article 25, the conditions for its invocation were not meet in the case under adjudication. The BIT Argentina – United Kingdom does not contain any clause like Article XI BIT United States – Argentina. Significantly, in another dispute under the same BIT, the tribunal applied customary international law – as codified in Draft Article 25 – after dismissing the rather unconvincing argument of the Claimant that the United Kingdom has persistently objected it, *National Grid*, above n. 6, paras 255 ff.

[8] In general, see Z. Douglas, 'The Hybrid Foundations of Investment Treaty Arbitrations' *British Yearbook Int'l L.* (2003) 151

necessity under customary international law and under the BIT. The question will be discussed in Part V.

All Tribunals and the *ad hoc* Committee also agreed that Draft Article 25 functions as a secondary rule by precluding the wrongfulness of the measures adopted on grounds of necessity. Secondary rules has been defined by the ILC as referring to "the general conditions under international law for the State to be considered responsible for wrongful actions of omissions, and the legal consequences which flow therefrom"[9]. Hence, necessity, alongside with other circumstances precluding wrongfulness, provides "a shield against an otherwise well-founded claim for the breach of an international obligation" [10].

Heavily relying on the ILC work, the *CMS* Tribunal constructed Draft Article 25 as a secondary rule by holding that (*prima facie*) breaches of the Treaty may be "devoid of legal consequences by the preclusion of wrongfulness" [11]. The *CMS ad hoc* Committee confirmed that Draft Article 25 is "an excuse which is only relevant once it has been decided that there has otherwise been a breach of […] substantive rules" [12].

In *Sempra*, the Tribunal held that Draft Article 25 could "foreclose any wrongfulness on the part of measures adopted [on ground of necessity] and […] exempt the State from international responsibility" [13]. Similarly, the *Continental* Tribunal held that:

> an act otherwise in breach of an international obligation ("not in conformity" with it) is not considered wrongful, and does not therefore entail the secondary obligations attached to an illicit act, thank to the "exceptional" presence of one of the conditions that under international law preclude wrongfulness, here necessity [14].

The application of Draft Article 25 in the above referred cases is convincing. Unlike primary rules, Draft Article 25 does not define the content of the substantive obligations imposed by the treaty. Rather, it *temporally* affects the effectiveness of the primary rule not complied with on grounds of necessity by releasing the State from the relevant obligations (exculpation) [15]. Consequently, there is no breach of the treaty. As explained by the ILC,

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[9] General commentary, para 1,.

[10] Commentary to Chapter V (Circumstances precluding wrongfulness), para 1.

[11] *CMS*, para 318.

[12] Para 129. It nonetheless did not exclude in categorical terms that Draft Article 25 could be treated as a primary rule, para 133.

[13] See also *LG&E*, para 245 ff.; *Enron*, para 288 ff.

[14] Para 166 *in fine*.

[15] According to V. Lowe, 'Precluding Wrongfulness or Responsibility: A Plea for Excuses', 10 *EJIL* (1999) 405, at p. 406, 'Exculpation operates by releasing a state from the obligation in question, so that

> [w]hen any one of these circumstances is present in a particular case, the wrongfulness of the act of the State is exceptionally precluded because in that instance, by reason of the special circumstances involved, the State taking the action is *no longer* obliged to act otherwise. From this point of view, there are no differences between any of the circumstances dealt with in the present chapter. The exceptional character lies precisely in the fact that the circumstance found to be present in the specific case in question renders *ineffective* an international obligation which, in the absence of that circumstance, would be incumbent on the State and would make any conduct that was not in conformity with the requirements of the obligation wrongful [16].

Hence, the concerned State may deliberately and at its own risk decides to adopt measures that would normally be inconsistent with its international obligation but are permitted on grounds of necessity, provided that all the conditions required under customary international law are satisfied [17].

IV. Legal nature of Article XI BIT

The legal nature of Article XI of the BIT was much more controversial. Article XI reads:

> This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests [18].

The *CMS*, *Enron* and *Sempra* tribunals construed it as a secondary rule. The *LG&E* tribunal shared the same opinion. It held that "Article XI establishes the state of

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the conduct incompatible with that obligation is not wrongful in those special circumstances'. For practical reasons, however, he would prefer the excusing – rather precluding wrongfulness – technique.

[16] 31 *YBILC* (1979-II) Part Two, p. 109 (italics added). Already in 1973, the ILC stated that when a State invoke circumstances precluding wrongfulness – such as necessity – "its conduct does not constitute an international wrongful act because, in those circumstances, the State is not required to comply with the international obligation which it would normally have to respect, so that there cannot be a breach of that obligation. Consequently, one of the essential conditions for the existence of an international wrongful act is absent", 25 *YBILC* (1973-vol. II), p. 178. In *Gabcíkovo – Nagymaros*, above n. 6, para 101, the Court held that necessity "may only be invoked to exonerate from its responsibility a State which has failed to implement a treaty. Even if found justified, it does not terminate a Treaty; the Treaty may be ineffective as long as the condition of necessity continues to exist; it may in fact be dormant, but - unless the parties by mutual agreement terminate the treaty - it continues to exist. As soon as the state of necessity ceases to exist, the duty to comply with treaty obligations revives".

[17] J. Crawford, *2nd Report on State Responsibility*, A/CN.4/498/Add. 2, 27-28, argues that "when a State invokes the state of necessity, it has full knowledge of the fact that it deliberately chooses a procedure that does not abide an international obligation." (quoted with approval by the *CMS Ad hoc* Committee, footnote to para 166).

[18] The treaty was signed on 14 November 1991 and entered into force on 20 October 1994. It is available at www.unctadxi.org/templates/DocSearch____779.aspx

necessity as a ground for exclusion from wrongfulness of an act of the State, and therefore, the State is exempted from liability" [19]. It further stressed the temporary character of the exemption since once the emergency situations has been overcome, the host State must immediately resume compliance with its international obligations [20].

The *CMS ad hoc* Committee strongly criticized the assimilation of Article XI and Draft Article 25. It held that the former is a primary rule whose application excludes the application of the substantive rules contained in the treaty. In the words of the Committee, that "Article XI is a threshold requirement: if it applies, the substantive obligations under the Treaty do not apply" [21].

Following the annulment decision in *CMS*, the *Continental* Tribunal clearly differentiated Article XI from Draft Article 25. The former is treated as a primary rule which "*restricts* or *derogates from* the substantial obligations undertaken by the parties to the BIT in so far as the conditions of its invocation are met" [22]. Therefore, if the conditions imposed by Article XI are satisfied, there is no need to examine the alleged breaches of the obligations imposed by the BIT. The decision of the *Continental* Tribunal to determine whether Article XI could be invoked before considering any *prima facie* breach of the BIT must be stressed for the fact that the Respondent invoked necessity only alternatively in the event the Tribunal would find breaches of the BIT.

It is submitted that the construction of Article XI offered by the *ad hoc* Committee and the *Continental* Tribunal correctly reflects the text and the object of Article XI. Contracting parties agreed that the right to adopt measures on grounds of necessity would not be affected by any provision of the treaty. In other terms, Article XI delimits the content of the other substantive provisions and the application of the former excludes any breach of the latter.

This position is reminiscent of that maintained by the United States before the ICJ in the *Oil Platforms* case in respect to Article XX, para 1 (d) of the 1955 Treaty of Amity, Economic Relations and Consular Rights between the United States and Iran, a provision similar to Article XI of the BIT between Argentina and the United States [23]. For the United States, the provision operated as a primary rule by *defining* and

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[19] *LG&E*, para 261. In para 229 it held that Argentina was *excused* under Article XI from liability for any breaches of the Treaty between 1 December 2001 and 26 April 2003.

[20] *Ibidem*.

[21] Para 129.

[22] *Continental*, para 164 (Italics added).

[23] *Case Concerning Oil Platforms*, Merits, *I.C.J. Reports 2003*, p. 161.

delimiting the obligation of the parties, "simultaneously with and on the same level as the other substantive rules" [24].

Without expressly accepting this position, in the *Oil Platforms* the Court seems incline to treat Article XX, para 1 (d) as a primary rule [25] when it conceded that

> If in the present case the Court is satisfied by the argument of the United States that the actions against the oil platforms were, in the circumstances of the case, "measures . . . necessary to protect [the] essential security interests" of the United States, within the meaning of Article XX, paragraph 1 (*d*), of the 1955 Treaty, it must hold that no breach of Article X, paragraph 1, of the Treaty has been established [26].

The Court decided to deal first with the application of the necessity clause and *then* with the alleged violations of the treaty [27]. It pointed out by the Court itself, there is no absolute need to consider first the alleged breaches of the treaty and then, if appropriate, interpret and apply the necessary measures provision. This pertains to the Court's exercise of "freedom to select the grounds upon which it will base its judgement" [28]. The decision attracted a good deal of criticism by several judges writing separate opinions [29].

Significantly, in *Nicaragua* the ICJ followed the opposite order in regard to a comparable clause, namely Article XXI, para 1, (d) of the 1956 Treaty of Friendship, Commerce and Navigation between the United States and Nicaragua. In this case, the Court seems to prefer characterising this clause as a secondary rule. It held that Article XXI, para 1, (d)

> [c]ontains a power for each of the parties to *derogate from* the other provisions of the Treaty, the possibility of invoking the clauses of that Article must be considered once it is

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[24] Para 36. In his intervention before the Court as Counsel for the United States, P. Weil argued that "*Article XX is a substantive provision which, concurrently and concomitantly with Article X, determines, defines and delimits the obligations of the parties*" (Italics as in the original), CR 2003/12, Wednesday 26 February 2003, 10 AM, available at http://www.icj-cij.org/docket/files/90/5159.pdf.

[25] In this sense, *CMS Ad hoc* Committee, para 133. According to J. Alvarez, K. Khamsi, above n. 4, p. 53, on the contrary, the ICJ at no time categorized Article XX, para 1 (d) as a primary rule.

[26] Para 34.

[27] Para 37.

[28] The Court relied here on *Application of the Convention of 1902 Governing the Guardianship of Infants*, Judgment, *I.C.J. Reports 1958*, p. 55, at p. 62.

[29] Judge Buergenthal, sep. op., para 5, for instance, maintained that Article XX, paragraph 1 (d), is intended to come into play or is relevant only if a party to the Treaty is found to have violated one of its substantive provisions". See also the separate opinions of Judges Higgins, para 34; Parra-Aranguren, para 13; Kooijmans, para 3, Owada, paras 5 ff.

> apparent that certain forms of conduct by the United States would otherwise be in conflict with the relevant provisions of the Treaty [30].

It then held that '[i]n so far as acts of the Respondent may appear to constitute violations of the relevant rules of law, the Court will then have to determine whether there are present any circumstances excluding unlawfulness' [31].

It is submitted that the pragmatic choice of the Court – especially in the *Oil Platforms* case – not to engage in theoretical discussion on the primary or secondary character of the relevant necessity clause demonstrates that the distinction is a relative one. Yet, either by affecting the content of the substantive provisions contained in the treaty (primary rule), or by rendering them temporally ineffective (secondary rule), these clauses produce in good substance the same effects.

In both cases, necessity amounts to a defence at the disposal of the Respondent at the merits stage [32]. As explained by the ICJ in the *Nicaragua* case, the question of admissibility depends on the jurisdictional clause contained in the treaty. In that case, as in the *Oil Platforms* case, the jurisdictional covered *any* dispute about the interpretation and application of the treaty, including those concerning Article XX, para 1 (d), regardless to its qualification as primary or secondary rule [33].

In both cases, if the plea is successful, the concerned State has committed no breach of international law. Therefore, no obligation arises to make reparation in general or to pay compensation in particular. Conversely, an unsuccessful necessity plea would unavoidably imply a violation of international law and attract the responsibility of the concerned State.

The distinction nonetheless is still relevant with regard to the order in which a tribunal may decide to proceed. If the relevant clause is treated as a primary rule, the tribunal has two options: to apply first the necessity clause and then, if required, establish any breach of the treaty; or to find provisionally any breach of the treaty and then considered the necessity plea. Otherwise the necessity plea is considered once the tribunal has found *prima facie* violations of international law.

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[30] *Case Concerning Military and Paramilitary Activities in and against Nicaragua*, Merits, *I.C.J. Reports 1986*, p. 14, para 225 (Italics added). Interestingly, the verb "to derogate from" was also used by the *Continental* Tribunal, above n. 22.

[31] Para 226.

[32] The *Continental* Tribunal, above n. 2, para 160, describes necessity under Article XI and under Draft Article 25 as two defences.

[33] Above n. 30, para 222. The Court held that "Article XXI defines the instances in which the Treaty itself provides for exceptions to the generality of its other provisions, but it by no means removes the interpretation and application of that article from the jurisdiction of the Court as contemplated in Article XXIV". See also *Oil Platforms* Case, above n. 23, para 33.

V. Co-ordination of Article XI BIT and Draft Article 25

If it is accepted that customary international law may be invoked by the host State even in the presence of a treaty provision on necessity (such as Article XI BIT United States – Argentina), the problem becomes the co-ordination of the two sources. The five tribunals and the *ad hoc* Committee approached the application of Article XI and Draft Article 25 in different ways [34].

The *CMS*, *Enron* and *Sempra* tribunals, after establishing *prima facie* that Argentina had breached certain provisions of the BIT, examined and rejected the necessity plea first under customary international law, as codified in Draft Article 25, then under Article XI of the BIT.

In *CMS*, in particular, the Tribunal dismissed the necessity plea under customary law as it found that not all the cumulative conditions imposed in Article 25 had been met. When dealing with the plea under Article XI, it held that it was entitled to substantially review Argentina's conduct, but eventually refrain to do so, presumably on basis of the undemonstrated assumption that customary international law and Article XI operate in the same manner and under the same conditions.

In the decision on annulment of the *CMS* award, the *ad hoc* Committee sharply criticized the Tribunal on many respects. It nonetheless held that the Tribunal sufficiently stated the reasons of the award and did not manifestly exceed its powers. On the one hand, it condoned the Tribunal for failing to analyse the necessity plea under Article XI since both parties accepted that the application of Article XI was essentially subject to the same conditions existing under customary international law [35]. On the other hand, the Committee expressed concern on the co-ordination of customary law and Article XI. For the Committee, the Tribunal should have applied Article XI as *lex specialis* and only subsidiarily customary law, regardless to the construction of the latter as primary or secondary rules. Given its narrow jurisdiction under Article 52 of the ICSID Convention, however, the Committee concluded that in spite of several errors and lacunas in the decision, the Tribunal had – however cryptically and defectively – applied Article XI and therefore there was no manifest excess of power.

The *Enron* and *Sempra* tribunal – which rendered their awards, respectively, before or days after the *CMS* annulment decision – substantially followed *CMS* on the issue of necessity in applying first customary international law and then Article XI. Their position on the co-ordination of customary law and Article XI is more articulated. Both Tribunals accepted that Article XI would in principle be *lex specialis*

[34] The following cursory description of the decisions does not follow the chronological order.

[35] Para 123.

[36]. Since this provision is silent on the conditions under which the host State could adopt measures on grounds of necessity, however, resort must be made to customary international law. They concluded that Article XI became "inseparable from the customary law standard insofar as the conditions for the operation of state of necessity are concerned" [37].

Also the *LG&E* Tribunal examined the necessity plea after finding certain *prima facie* breaches of the BIT. Unlike the *CMS*, *Enron* and *Sempra* tribunals, however, it focused on Article XI. It held that during the period between 1 December 2001 and 26 April 2003 all the conditions required for the invocation Article XI were satisfied and therefore the measures adopted by Argentina on grounds of necessity did not engage its responsibility [38]. It nonetheless considered also Draft Article 25 and held that the customary international rules governing necessity support the conclusion reached in respect to Article XI [39].

In *Continental*, the Tribunal approached the question of necessity in a completely different way. On the one hand, it addressed the question of necessity *before* examining the individual claims of breach of the BIT [40]. On the other hand, building on the *CMS* decision on annulment [41], it emphasized that the conditions for the adoption of measures on grounds of necessity required under Article XI and Draft Article 25 are not the same [42]. It nonetheless conceded that Draft Article 25 may "assist" in the interpretation of Article XI [43].

The order in which Article XI and Draft Article 25 have been applied in *LG&E* and *Continental* is clearly to be preferred. A treaty – and especially a bilateral one – being *lex specialis* has "inherent priority over such rules of a general nature" that may also be applicable between the parties [44]. The principle is well-established across international law [45], including investment law [46]. This does not imply any formal

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[36] They held that "a treaty regime specifically dealing with a given matter will prevail over more general rules of customary law", *Enron*, para 334 and *Sempra*, para 376.

[37] *Enron*, para 334. See also *Sempra*, para 376.

[38] *LG&E*, paras 229 ff.

[39] *LG&E*, para 245.

[40] *Continental*, para 161.

[41] *CMS*, Annulment, especially para 129.

[42] *Continental*, para 163.

[43] *Continental*, para 168.

[44] R. Ago, dissenting opinion, *Interpretation of the Agreement of 25 March 1951 between the WHO and Egypt*, Advisory Opinion, *I.C.J. Reports 1980*, p. 73, at p. 162.

[45] See, for instance, *Gabcíkovo – Nagymaros*, above n. 6; *Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory*, Advisory Opinion, *I. C. J. Reports 2004*, p. 136, para 140.

[46] In *ADC Affiliate Limited and ADC & ADMC Management Limited v. Hungary*, ICSID ARB/03/16, Award, 2 October 2006, para 481, in particular, the Tribunal held that 'there is general authority for the

hierarchy between treaty and customary rules and is without prejudice to the intense and continuous interaction between the two sources.

Accordingly, necessity in the five cases under discussion is first and foremost a question of interpretation and application of Article XI. Tribunals should have started by ascertaining the meaning of Article XI in accordance with the relevant rules on treaty interpretation, taking into account *inter alia* any rule of international law applicable between the parties, including customary international law and general principles of law [47].

Equally important, the priority established by the *lex specialis* operates to the extent the treaty provision and customary international law are inconsistent. Accordingly, Draft Article 25 continues to be applicable insofar as it does not conflict with Article XI [48]. The mere inclusion of a necessity clause in a BIT does not preclude the application Draft Article 25, even if the two texts are not identical. Customary law ceases to be applicable when the relevant treaty provision departs from it or excludes its applicability [49].

Moreover, international customary law may contribute – alongside general principles of law – to fill the gaps and lacunae of Article XI. An ICSID Tribunal has convincingly held that when

> the BIT does not contain any *lex specialis* rules that govern the issue of the standard for assessing damages in the case of an unlawful expropriation, the Tribunal is required to apply the default standard contained in customary international law in the present case [50]

Such a possibility is well established in international law [51] and has been confirmed expressly in Article 55 of the Draft Articles on State Responsibility [52].

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view that a BIT can be considered as *lex specialis*'. See also *Phillips Petroleum Co. Iran* v. *Iran*, 29 June 1989, 21 *Iran-U.S.C.T.Rep*. 79, para 107. See also: *Amoco Int. Finance Corp*. v. *Islamic Republic of Iran et al*., Iran-U.S.C.T., 14 July 1987, 83 *ILR* (1990) 500, para 112; *ADF* v. *United States*, ICSID ARB (AF)/00/1, Award, 9 January 2003, para 147.

[47] See C. McLachlan, 'The Principle of Systemic Integration and Article 31 (3) (c) of the Vienna Convention', 54 *ICLQ* (2005) 279.

[48] *CMS*, para 350; *Enron*, para 335; *Sempra*, para 378.

[49] See also J. Alvarez, K. Khamsi, above n. 4, especially p. 44, p. 48 and p. 50. The two authors, however, seems to assimilate primary rules and *lex specialis* (p. 49 and p. 53). It is argued that the distinction must be kept. A primary rule contained in a treaty defines the content of international obligations. It may depart from, or be consistent with customary international rules, assuming there are any governing the same subject matter. It is only in case of inconsistency that the *lex specialis* principle is relevant. Far from introducing a self-contained regime, the principle concerns the co-ordination of rules stemming from different sources.

[50] *ADC and ADC & ADMC* v. *Hungary*, above n. 46, para 483. See also *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v. Mexico*, ICSID ARB (AF)/04/5 (NAFTA), Award (Redacted Version), 21 November 2007, para 119.

VI. Non self-judging character of Article XI

Before discussing the conditions under which the host State can invoke Article XI of the BIT between Argentina and the United States, however, it is appropriate to briefly discuss which kind of control an arbitral tribunal is entitled to exercise over the respect of these conditions.

In the five cases under examination, Argentina argued that Article XI is a self-judging provision and that it is for the host State to determine in good faith whether essential security interests are at stake and what measures are necessary to protect them. According to Argentina, this interpretation of Article XI is shared by *both* parties to the treaty and is firmly based on reciprocity.

Argentina maintained that since the *Nicaragua* decision [53] – or at least after the conclusion of the BIT between the United States and Argentina [54] – the United States have consistently treated clauses on emergency measures as self-judging as demonstrated *inter alia* by the BITs concluded by the United States with Russia (1992) [55] and Bahrain (1999) [56] as well as the current Model Treaty (2004) [57]. Argentina also relied on several official documents of the United States Congress. In *Sempra* and *Continental*, it also relied on a letter sent on 15 September 2006 by an official of the

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[51] In *Amoco International Finance Corporation v. Iran*, Iran-US. C.T.R., vol. 15 1987-II, p. 222, the Iran – US Claims Tribunal found that '[a]s a *lex specialis* in the relations between the two countries, the Treaty supersedes the *lex generalis*, namely customary international law. This does not mean, however, that the latter is irrelevant in the instant Case. On the contrary, the rules of customary law may be useful in order to fill in possible lacunae of the Treaty, to ascertain the meaning of undefined terms in its text or, more generally, to aid interpretation and implementation of its provision'.

[52] Draft Articles, above n. 6.

[53] *CMS*, para 350; *Continental*, para 186.

[54] *LG&E*, para 209.

[55] In the Protocol to the treaty, reproduced in 31 *Int.l Legal Materials* (1992) 794, p. 811, the parties confirmed their mutual understanding that whether a measure is undertaken by a Party to protect its essential security interests is self–judging. The treaty is not in force.

[56] Available at www.unctadxi.org/templates/DocSearch____779.aspx. According to Article 14 (1), the treaty "shall not preclude a Party from applying measures which it considers necessary for the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests". The Letter of submittal to the Congress on this point reads: "This Treaty makes explicit the implicit understanding that measures to protect a Party's essential security interests are self-judging in nature, although each Party would expect the provisions to be applied by the other in good faith".

[57] Available at http://ita.law.uvic.ca/documents/USmodelbitnov04.pdf. According to Article 18 (2), a contracting party is allowed to take the measures *it considers necessary* to protect *inter alia* its *own* essential security interests.

Department of State to a former official testifying in the context of a different arbitration [58].

All tribunals convincingly rejected the argument. In their opinion, Article XI cannot be considered self-judging due to the silence of the treaty and the absence of any contextual element imposing such an interpretation [59]. The finding was supported by references to the ICJ judgments in the *Nicaragua* [60], *Oil Platforms* [61] and *Gabcikovo-Nagymaros* [62] cases.

All tribunals also pointed out that nothing would prevent contracting parties from leaving each of them to determine what is a measure necessary to protect its essential security interests. Indeed, this has occurred in respect of other BITs [63]. Due to the exceptional or extraordinary character of the measures adopted on grounds of necessity, however, the self-judging character of the relevant provisions contained in BITs cannot be presumed but must be expressed in the text of the treaty [64].

With regard to the ordinary meaning to be given to the terms of Article XI [65], the use of the expression "measures necessary" and not "measures the host State considers as necessary", as in the case of similar provisions in other treaties, clearly militates against the self-judging argument. This is also respectful of the agreement of the parties to have disputes concerning the treaty settled compulsorily by arbitration [66].

The finding is not affected by the subsequent practice of the parties as maintained by Argentina and in literature [67]. Under article 31 (3) (b) VCLT, the interpreter should

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[58] *Sempra*, para 382; *Continental*, footnote 278.

[59] *CMS*, paras 332 ff.; *LG&E*, paras 207 ff.; *Enron*, paras 324 ff.; *Sempra*, paras 366 ff.; *Continental* paras 182 ff. In *LG&E*, para 213, however, the Tribunal noted that substantial review and good faith review would not differ significantly.

[60] Above n. 30, paras 222 and 282.

[61] Above n. 23, para 43.

[62] Above n. 6, para 51.

[63] See, for instance, the BITs referred to above notes 55 and 56.

[64] *CMS*, para 370. In *Enron*, para 336, and *Sempra*, para 383, it has been held that the provision must be "very precise" in order to establish its self-judging nature. In *Sempra*, para 379, the Tribunal further added that "[t]ruly exceptional and extraordinary clauses, such as a self-judging provision, must be expressly drafted to reflect that intent, as otherwise there can well be a presumption that they do not have such meaning in view of their exceptional nature".

[65] In *Territorial Dispute* (Libyan Arab Jamahiriya/Chad), Judgment, *I.C.J. Reports 1994*, p. 6, para 41, the ICJ confirmed that "[i]nterpretation must be based above all upon the text of the treaty".

[66] As emphasized in *Continental*, para 187.

[67] W. Burke-White, A. von Staden, above n. 4, p. 368 ff. For a full discussion of United States practice, see J. Alvarez, K. Khamsi, above n. 4, p. 34 ff., who convincingly argue that such a practice, including the conclusion of BITs, clearly militates against the self-judging interpretation of Article XI.

take into account any subsequent practice *in the application of the treaty* establishing the agreement *of the parties* regarding *its* interpretation [68]. Accordingly, the inclusion of self-judging clauses in BITs concluded by the United States with other States has little or no significance for the purpose of interpreting Article IX of the BIT between Argentina and the United States. [69].

Finally, it is important to stress that subsequent practice leading to a modification of a treaty provision should be taken into account only up to the commission of the acts allegedly in violation of the treaty [70]. The parties to a BIT can at any time informally modify it through subsequent practice. For the purpose of interpreting and applying a provision in the settlement of a given dispute, nonetheless, it is indispensable to determine whether subsequent practice has led to the modification of the said provision *at the time* of the conduct the foreign investor is complaining about.

As pointed out by the *Enron* and *Sempra* tribunals,

> [e]ven if [the self-judging] interpretation were shared today by both parties to the Treaty, it would still not result in a change of its terms. States are of course free to amend the Treaty by consenting to another text, but this would not affect rights acquired under the Treaty by investors or other beneficiaries [71].

Safeguarding the foreign investor against any retroactive effect of subsequent practice is indeed indispensable in international investment law, where the parties to the treaty and those to the dispute do not coincide, if the rights acquired under the treaty by the foreign investor are to be adequately protected within a stable and predictable legal framework.

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[68] See *Kasikili/Sedudu Island, (Botswana/Namibia)*, Judgment, *I.C.J. Reports. 1999*, p. 1045, esp. paras 49-50. As noted by the ILC, 18 *Yearbook ILC* (1966-II), p. 221, '[t]he importance of such subsequent practice in the application of the treaty, as an element of interpretation, is obvious; for it constitutes objective evidence of the understanding of the parties as to the meaning of the treaty. Recourse to it as a means of interpretation is well-established in the jurisprudence of international tribunals'.

[69] Given the *res inter alios acta* character of treaties, reliance on these treaties must be treated with the greatest prudence. See, in particular, *Ceskoslovenska Obchodni Banka, a.s. v. Slovak Republic,* ICSID ARB/97/4, Jurisdiction, 24 May 1999, para 57.

[70] The difficulties related to the distinction between interpretations and amendments are demonstrated by the debate provoked by NAFTA Free Trade Commission, *Notes of Interpretation of Certain Chapter 11 Provisions*, 31 July 2001, at http://www.naftaclaims.com/files/NAFTA_Comm_1105_Transparency.pdf. For a sharp critique of the Commission interpretation see *Second Opinion of Professor R. Jennings*, in *Methanex Corporation* v *United States*, UNCITRAL (NAFTA), available at available at http://www.naftaclaims.com/disputes_us_methanex.htm.

[71] *Enron*, para 337; *Sempra*, para 385. The statement would have been clearer had it specified in the first sentence that no change would have resulted "for the purpose of this dispute".

VII. Economic crisis as a threat to the essential security interests of the host State

The crux of the matter in the five cases under discussion remains the conditions under which the host State can invoke Article XI. The provision merely indicates that measures can be adopted on grounds of necessary for (a) the maintenance of public order; (b) the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security; or (c) the protection of its own essential security interests.

All five tribunals agreed that a serious economic crisis may be qualified as a threat to the essential security interests of a State for the purpose of Article XI BIT. In the words of the Tribunal in *Continental*, for example, the host State is allowed under Article XI to take

> actions properly necessary by the central government to preserve or to restore civil peace and the normal life of society (especially of a democratic society such [as] that of Argentina), to prevent and repress illegal actions and disturbances that may infringe such civil peace and potentially threaten the legal order, even when due to significant economic and social difficulties, and therefore to cope with and aim at removing these difficulties, do fall within the application under Art. XI [72].

The problem is then to establish how serious the economic crisis must be in order to trigger the application of Article XI. All tribunals agreed that the situation must be exceptional. In *LG&E*, for instance, the Tribunal held that the "emergency periods should be only strictly exceptional and should be applied exclusively when faced with extraordinary circumstances" [73]. With respect to the crisis in Argentina, it decided that the situation was grave enough to justify the adoption of measures on grounds of necessity as from 1 December 2001, when the adoption of the Decree of Necessity and Emergency

> triggered widespread social discontent. Widespread violent demonstrations and protests brought the economy to a halt, including effectively shutting down transportation systems. Looting and rioting followed in which tens of people were killed as the conditions in the country approached anarchy. A curfew was imposed to curb lootings [74].

The exceptional nature of the situation, allowing Argentina to invoke Article XI, clearly transpires throughout the whole *Continental* award as well. The description of

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[72] Para 174. See also *CMS*, para 359; *LG&E*, para 238; *Enron*, para 332; *Sempra*, para 374.

[73] Para 228.

[74] Para 235. In *LG&E*, para 238, the Tribunal held that "State's economic foundation is under siege, the severity of the problem can equal that of any military invasion". In para 231, the Tribunal held that the "extremely" severe" crisis was threatening "total collapse of the Government and the Argentine State". See also *CMS*, para 317; *Enron*, para 304; *Sempra*, para 345.

the situation offered by the Tribunal leaves no doubt about the proportions and dangers of the crisis. The Tribunal held that the crisis

> brought about the sudden and chaotic abandonment of the cardinal tenet of the country's economic life, […]; the near collapse of the domestic economy; the soaring inflation; the leap in unemployment; the social hardships bringing down more than half of the population below the poverty line; the immediate threats to the health of young children, the sick and the most vulnerable members of the population, the widespread unrest and disorders; the real risk of insurrection and extreme political disturbances, the abrupt resignations of successive Presidents and the collapse of the Government, together with a partial breakdown of the political institutions and an extended vacuum of power; the resort to emergency legislation granting extraordinary legislative powers to the executive branch [75].

Significantly, one of the reasons indicated by the *Continental* Tribunal for rejecting the necessity plea in respect of the measures concerning LETE was precisely because at the time of the adoption of these measures "conditions were evolving towards normality" [76].

The five tribunals, however, disagreed on whether the economic crisis in Argentina could justify the adoption of measures on grounds of necessity. The *CMS*, *Enron* and *Sempra* tribunals dealt with the question in a rather cursorily manner and apparently found that measures on grounds of necessity can be adopted only in situation of total collapse. The *CSM* Tribunal, in particular, held that

> A severe crisis cannot necessarily be equated with a situation of total collapse. And in the absence of such profoundly serious conditions it is plainly clear that the Treaty will prevail over any plea of necessity. [77]

The finding that the crisis in Argentina "was severe but did not result in total economic and social collapse" [78] was one of the main reasons for the rejection by the Tribunal of the necessity plea. According to the *Enron* and *Sempra* Tribunals, in turn, a situation can be qualified as involving an essential interest of the State when it compromises the very existence of the State and its independence [79].

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[75] Para 180. The award contain several references to "severe" (para 178), "major" (para 178) or "grave" (para 181) economic crises and even to the need "to prevent the complete break-down of the financial system" (para 197). It must nonetheless be noted that in para. 167 the Tribunal observed that if a necessity plea can be accepted under customary international law only on an exceptional basis, this is not necessarily the case of treaty provisions.

[76] Para 221.

[77] Para 354.

[78] Para 355. In para 322, the Tribunal nonetheless conceded that there was a "danger of total economic collapse".

[79] *Enron*, para 306; *Sempra*, para 347.

For the *LG&E* and *Continental* Tribunals, in contrast, a State is entitled to adopt measures on grounds of necessity in order to prevent the degeneration of the situation into the total collapse of the economy. For the first tribunal,

> [t]he concept of state of necessity and the requirements for its admissibility lead to the idea of prevention: the State covers itself against the risk of suffering certain damages. Hence, the possibility of alleging the state of necessity is closely bound by the requirement that there should be a serious and imminent threat and no means to avoid it [80].

The second tribunal further held that

> [t]he protection of essential security interests recognized by Art. XI does not require that "total collapse" of the country or that a "catastrophic situation" has already occurred before responsible national authorities may have recourse to its protection. The invocation of the clause does not require that the situation has already degenerated into one that calls for the suspension of constitutional guarantees and fundamental liberties. There is no point in having such protection if there is nothing left to protect [81].

The threshold put by the *CMS*, *Enron* and *Sempra* tribunals cannot be accepted. Necessity measures would hardly have any chance to be effective if they can be adopted only when the total collapse of the economy is unavoidable or the very existence of the State compromised. As explained in *LG&E* and *Continental*, these measures are intended to preserve the essential interests of the host State and must be adopted before the situation goes out of control or is irreversible.

Rather than "total economic or social collapse", the notion of "grave and imminent peril" contained in Draft Article 25 should guide the tribunal in interpreting and applying Article XI. The existence of a "grave and imminent peril" is precisely the essence of any measures adopted on grounds of necessity. From this perspective, customary international law fill the gaps and lacunae of Article XI which laconically permit a State to protect to protect its own essentially security interests without defining them nor specifying against what they could be protected.

The test requires a careful assessment of all relevant economic, social and political aspects of and the dangers posed by the crisis [82]. The analysis contained in *Continental*, in particular, is based on several different sources – including most prominently the IMF 2004 Evaluation Report, several other IMF official documents and occasional research papers – and provides enough evidence to qualify the crisis

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[80] Para 248.

[81] See *Continental* , para 180.

[82] In *LG&E*, para 248 the Tribunal held that '[a]ll of these devastating conditions – economic, political, social – in the aggregate triggered the protection afforded under Article XI of the Treaty to maintain order and control the civil unrest'.

that hit Argentina as serious enough to trigger the application of Article XI. In the words of the Tribunal

> The immediate macroeconomics consequences of crisis were severe. the Real GDP fell by about 10% in 2002, bringing the cumulative decline since 1998 to almost 20%. Inflation peaked at a monthly rate of about 10% in April 2002, driven by liquidity provisions from the central bank to banks experiencing deposit withdrawals, but then declined, averaging around 40% for the year as a whole. More generally the crisis was characterized by severe deflation, a decline in domestic prices as a consequence of the peso overvaluation and the deterioration of the competitiveness of the economy. The stock index of Buenos Aires lost more than 60% from 1998 to 2002. […] the crisis lead to substantial social and personal hardship, including the youngest and most vulnerable members of the populations: the unemployment rate rose to above 20% in 2002; and per capita expenses fell off about 74%. The poverty level increased to 54.3% of the urban population of the country and the indigence level reached 24.7%. Between October 1998 and October 2002, the poverty level was doubled, whereas the indigence level increased 358%," most of the increase having taken place from May 2001 on. Argentina also points out to other aspects of the social crisis due to the "impossibility of the State to provide the necessary conditions for harmonious development of society as set forth in the Argentine Constitution," due to the gradual deterioration of the State as regards fulfillment of security and health duties. The political effects of this massive economic and social crisis, were "the political demonstrations, riots and looting in December 2001 which led to an abrupt end of De La Rúa's government" and the vacuum in the political power that followed his resignation. Argentina has concluded from its recapitulation of those events that "the effective control of the government on the territory was seriously endangered, with presidents coming one after the other and riots causing tens [sic] of deaths throughout the country, which entails in turn that the existence of the Argentine Government137 itself was at risk."138 The Tribunal accepts this characterization of the gravity of the crisis confronting Argentina at this particular time [83].

It is submitted that due to the combined effects of all these economic, social and political elements the crisis in Argentina reached the threshold required in Article XI for the adoption of measures on grounds of necessity.

VIII. Non-contribution to the creation of the emergency situation

Draft Article 25 cannot be invoked by a State that has contributed to the situation of necessity. It remains to be seen whether such a condition equally applies to Article XI in spite of the silence of this provision.

The non-contribution requirement has been discussed by four tribunals with regard to Draft Article 25. Three tribunals held that Argentina "substantially" contributed to the crisis. The *Enron* Tribunal, for instance, held that

[83] Para 108 (footnotes omitted).

> there has been a substantial contribution of the State to the situation of necessity and that it cannot be claimed that the burden falls entirely on exogenous factors. This has not been the making of a particular administration as it is a problem that had been compounding its effects for a decade, but still the State must answer as a whole [84].

This finding – alongside the qualification of the crisis described in the previous section – precluded the invocation by the Respondent of state of necessity. These tribunals however did not explain the qualification of the contribution as "substantial" nor provide any serious evidence on the responsibility of Argentina in the crisis.

Another tribunal reached the opposite conclusion. In this case too the Tribunal is rather laconic and limits itself to observe that

> in the first place, Claimants have not proved that Argentina has contributed to cause the severe crisis faced by the country; secondly, the attitude adopted by the Argentine Government has shown a desire to slow down by all the means available the severity of the crisis [85].

The position of the Tribunal in *Continental* is quite intriguing. The Tribunal seems first to hold that the non-contribution requirement applies to Draft Article 25 but not to Article XI [86]. It nonetheless admitted that had Argentina "contributed to endangering" its essential security interests, the measures would have no longer be considered as necessary and therefore invocation of Article XI precluded. The Tribunal did not elaborate on the meaning of "contribution to endangering", nor indicate in what this would be different from contribution in the sense of Draft Article 25.

Then, the Tribunal discussed whether Argentina could be defaulted for not having more energetically pursued the policies recommended by the IMF [87]. It answered in the negative and further clarified two important points. First, it resorted to a counter-factual approach and, relying on an IMF research paper, held that the crisis would not have been avoided even if Argentina had fully implemented the IMF recommendations. Second, it observed that Argentina made *reasonable efforts* to comply with its international obligations [88].

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[84] *Enron*, para 312. Similarly, see *Sempra*, para 354, when the Tribunal held that "there has to some extent been a substantial contribution of the State to the situation giving rise to the state of necessity". See also *CMS*, para 329.

[85] *LG&E*, para 256. Here the Tribunal imposed the burden of proof on the Claimant whereas traditionally such a burden is for the subject invoking State of necessity, see D. Anzilotti, separate opinion, *Oscar Chinn Case*, 12 December 1934, PCIJ Series A/B No. 63, p. 107.

[86] Para 234.

[87] *Continental*, para 226.

[88] *Continental*, para 227.

Furthermore, while determining whether there were any reasonable alternatives available to Argentina, the Tribunal looked both at

> i) alternatives to the Measures, not in breach of the BIT, that might have been available when the Measures challenged were taken (thus from November 2001 onwards) and that would have yielded equivalent results/relief; and
> ii) whether Argentina could have adopted at some earlier time different policies, that would have avoided or prevented the situation that brought about the adoption of the measures challenged [89] .

Only the first leg of the test is truly concerned with the question of the existence of alternatives. Whether alternative measures were available to the government must be determined with regard to the moment at which the measures concerned had been adopted. The test may be applied both globally with regard to these measures as whole and individually with regard to each of them. The second leg of the test, on the contrary, concerns the conduct of the host State in the period preceding the adoption of these measures. This test is global in character in the sense that it examines the conduct of Argentina with respect to the whole crisis. It aims at verifying whether the host State could have avoided or prevented the state of necessity.

It may be argued that all five Tribunals conditioned the applicability of Article XI to the satisfaction of the non-contribution requirement in spite of the silence of this provision. The *Continental* Tribunal apparently goes even further by holding that the host State is not only expected not to contribute to the crisis (negative obligation), but also to demonstrate due diligence by adopting the reasonable measures that could avoid or prevent it (positive obligation).

As far as the non-contribution requirement is concerned, this result is to be welcome since, as stressed in *Enron* and *Sempra*, the non-contribution requirement is "expression of a general principle of law devised to prevent a party taking legal advantage of its own fault" [90]. It is indeed logical to resort to a general principle of law recognized in virtually all legal systems in order to complete a provision as vague as Article XI and ensure its correct interpretation and application [91] .

The real challenge remains, first, to disentangle exogenous factors from conduct attributable to the government, and then, to assess whether and to what extent the

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[89] Para 198.

[90] *Enron*, para 311; *Sempra*, para 353.

[91] In *LG&E*, para 256, the Tribunal held that "[t]he State must not have contributed to the production of the state of necessity. It seems logical that if the State has contributed to cause the emergency, it should be prevented from invoking the state of necessity. If there is fault by the State, the exception disappears, since in such case the causal relationship between the State's act and the damage caused is produced".

government contributed to the crisis. A brutal repression of a peaceful demonstration that ignites serious social and political disturbances threatening the maintenance of public order and the breakdown of political institutions is a clear example of conduct that bars the invocation of Article XI.

Most of time, however, the State behaves more diligently and finding whether and to what extent it has contributed to the situation is much more problematic. Under the circumstances, the question may perhaps be more tractable if approached not in terms of positive contribution by the host State to the situation of crisis, but rather of incapacity or unwillingness to take the measures that could be reasonably be expected to be taken. As underlined in *Continental* [92], in crises like the one that hit Argentina, the readiness to follow the advice of the IMF and the attitude of the IMF itself may provide important indications for the assessment of the responsibilities of the host State [93].

The five tribunals assessed differently the responsibilities of the Argentine government in the management of the crisis. Beyond these divergences, nonetheless, there seems to be agreement insofar as contribution to the crisis would prevent the host State from invoking necessity not only under customary international law, but also under Article XI BIT.

IX. Lack of alternatives consistent with or less disruptive of the BIT

Under customary international law, a State cannot adopt measures on grounds of necessity unless they are the only means to safeguard its essential interests against a grave and imminent peril. Indeed, the lack of alternatives consistent with or less disruptive of the international obligations of the concerned State is the essence of necessity [94].

Article XI BIT Argentina - United States, in turn, merely refers to measures necessary for the protection of its own essential security interests without providing any definition of "necessary".

The five tribunals reached different conclusion on the necessity of the measures adopted by Argentina. This is partly due to their different approach to the co-ordination of Draft Article 25 and Article XI.

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[92] Para 223 ff.

[93] For a completely different reading of the IMF study, however, see *National Grid*, above n. 6, especially para 260. In this case, the Tribunal held that Argentina substantially contributed to the crisis and accordingly rejected the necessity plea under customary international law.

[94] Draft Article 25 (1) (a). According to D. Anzilotti, above n. 85, p. 114, 'the plea of necessity […] by definition, implies the impossibility of proceeding by any other method than the one contrary to law'. See also R. Ago, , *Addendum to the 8th Report on State Responsibility*, 32 *YBILC* (1980-II) Part 1, p. 49.

Three of them discussed the issue from the standpoint of customary international law. They did not accept that the measures adopted by Argentina were the only way to tackle the crisis by merely indicating that the disagreement among experts on the issue demonstrates the existence of several alternatives [95]. All of them refrained from assessing these alternatives as this would have implied passing a judgment on the economic policies of a sovereign government. Such deference is misplaced as it is precisely the task of the tribunal to check whether the conditions required in order to invoke necessity are satisfied and lack of alternative is one of them. Far from protecting the sovereign, furthermore, it is ultimately harmful to the government itself as the non-satisfaction of the no-alternative requirement was one of the two reasons for the rejection of the necessity claim.

Another tribunal focused on Article XI and held that it

> refers to situations in which a State has no choice but to act. A State may have several responses at its disposal to maintain public order or protect its essential security interests. In this sense, it is recognized that Argentina's suspension of the calculation of tariffs in U.S. dollars and the PPI adjustment of tariffs was a legitimate way of protecting its social and economic system [96].

Here the Tribunal waters down the no-alternative requirement to apply a softer test based on the "legitimacy" of the measures adopted without specifying either the origin or the nature of such a test. The impression is that the Tribunal is refraining from engaging in an analysis of the alternative and leaning to a mere control of good faith on the part of the host State [97].

The question of the existence of alternatives received a more detailed treatment in *Continental*. The Tribunal checked the existence of alternatives for the purpose of Article XI BIT against the standard developed in GATT and WTO case-law concerning Article XX GATT [98]. According to this standard, whether a measure is necessary for the purpose of Article XX must be determined through

> a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports [99].

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[95] *CMS*, para 323-4; *Enron*, para 308-9; *Sempra*, para 350-1.

[96] *LG&E*, para 239.

[97] Interestingly, the same Tribunal minimized the difference between substantial review and good faith review, see above n. 59.

[98] Para 192.

[99] Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, 10 January 2001, para 164. The *Continental* Tribunal preferred to

As explained by the Appellate Body in *United States – Gambling*, however, the outcome of the "weighing and balancing" process needs to be completed by a comparison between the measures assessed and the potential alternative measures. In the words of the Appellate Body,

> [a] comparison between the challenged measure and possible alternatives should then be undertaken, and the results of such comparison should be considered in the light of the importance of the interests at issue. It is on the basis of this "weighing and balancing" and comparison of measures, taking into account the interests or values at stake, that a panel determines whether a measure is "necessary" or, alternatively, whether another, WTO-consistent measure is "reasonably available" [100].

The *Continental* Tribunal first found in general terms that the whole package of measures adopted by Argentina was in part inevitable and in part indispensable to effectively tackle the crisis and that no reasonable alternatives were available [101]. It then identified four different categories of measures adopted by Argentina and considered whether there existed with respect to each of them any alternative consistent or less disruptive of the BIT. It held that the measures were inevitable, effective and adequate (bank freeze), simply inevitable (pesification of dollar-denominated contracts and deposits); appropriate and reasonable (suspension of payment with the exception of LETE). In respect of the devaluation of the peso it discussed two concrete alternatives allegedly available to Argentina. Both alternatives were dismissed as being of proven ineffectiveness (voluntary debt exchange) or purely theoretical and impracticable (full dollarization).

The application of the standard of necessity as developed in accordance with Article XX GATT to Article XI BIT deserves close scrutiny. It must be noted in the first place that GATT contains a provision on security exceptions. Article XXI GATT preserves the right of Members to take any action which they consider necessary for the protection of their essential security interests in time of war or "other emergency in international relations". Assuming that a severe economic crisis having serious repercussions beyond the borders of the concerned State may fall within definition of

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quote the most recent Panel Report in *Brazil – Measures Affecting Imports of Retreated Tyres*, WT/DS332/AB/R, adopted 12 June 2007, para 7.104 although in this report, unlike the Appellate Body reports referred to, the panel took into account the *relative* importance of the interests and values protected. See also the Appellate Body report, in *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R, 5 April 2001, para 172; *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/AB/R, 20 April 2005, paras 305-307; *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/AB/R, 19 May 2005, para 70.

[100] *United States –Gambling*, above n. 99, para 307.

[101] *Continental*, paras 197 ff.

"emergency in international relations", then Article XXI GATT is substantially comparable to Article XI BIT. This may militate against resorting to Article XX GATT for the purpose of interpreting and applying Article XI BIT.

In spite of some textual analogies, moreover, the general exceptions foreseen in Article XX GATT seem to respond to a different logic compared with Article XXI GATT or Article XI BIT. Under Article XX GATT a balance must be struck between the right of a Member to invoke Article XX GATT and the rights of other Members under the various substantive provisions of the treaty [102]. According to the Appellate Body,

> The task of interpreting and applying the chapeau is, hence, essentially the delicate one of locating and marking out a line of equilibrium between the right of a Member to invoke an exception under Article XX and the rights of the other Members under varying substantive provisions (e.g., Article XI) of the GATT 1994, so that neither of the competing rights will cancel out the other and thereby distort and nullify or impair the balance of rights and obligations constructed by the Members themselves in that Agreement. The location of the line of equilibrium, as expressed in the chapeau, is not fixed and unchanging; the line moves as the kind and the shape of the measures at stake vary and as the facts making up specific cases differ [103].

The reservations made above notwithstanding, Article XX GATT may provide some useful indications for the purpose of interpreting and applying Article XI BIT. Yet, it is a common feature of most international tribunals to borrow legal reasoning from each other, even if they are mandated to settle disputes in different areas or between different subjects. The cross-contamination of international decisions may contribute to the preservation of the coherence and unity of international law [104]. Such an approach is further justified if it is accepted that Article XI BIT derives from the parallel clause contained in Friendship, Commerce and Navigation treaties concluded by the United States, which in turn was inspired by Article XX GATT [105].

It is submitted that the two-tier exam developed in GATT/WTO case law [106] is not only to a large extent consistent with the rules governing necessity in customary international law, but also suitable for the purpose of establishing whether the measures adopted under Article XI BIT Argentina – United States were "necessary".

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[102] J. Alvarez above n. 4, p. 55, observes that "Article XX of the GATT is grounded in a balancing test that is absent from the text *U.S.-Argentina BIT*'s Article XI. Article XI suggests an on/off switch; either a measure is "necessary" for the stipulated reasons or it is not. Nothing in it suggests the balancing test implied in the preamble of the GATT's Article XX".

[103] Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, 6 November 1998, para 159.

[104] See R. Higgins, 'A Babel of Judicial Voices? Ruminations from the Bench', 55 *ICLQ* (2006) 791.

[105] In this sense, see *Continental*, para 192.

[106] Above text n. 99 and n. 100.

The first part of the exam is conducted in absolute terms, primarily on the basis of (a) the contribution of the measures to the realization of the ends for which they are engaged and (b) the impact of the legally protected interests of the foreign investor.

The contribution of the measures to the realization of the ends for which they are engaged, introduces in the notion of effectiveness. Being adopted under exceptional circumstances and amounting to a departure from normalcy, measures adopted on grounds of necessity are permitted only when they are expected to defuse the threat of economic or social collapse. From this perspective, the tribunal has to position itself at the moment of the adoption of these measures and to assess – on the basis of the evidence available at that time – their effectiveness in terms of the effects that they were reasonably expected to produce [107].

The impact of the measures adopted on grounds of necessity on the legally protected interests of the foreign investor introduces the notion of proportionality. Given the importance of the interests of the host State at stake, the measures adopted on grounds of necessity *as a whole* may hardly be disproportionate. The measures individually taken, however, are permitted on grounds of necessity only if they are proportionate to the specific objective they are intended to achieve.

The second part of the exam is conducted in comparative terms. The tribunal identifies any potential alternative measure – if any – and compare it with the one adopted by the host State, both in respect of their effectiveness and impact on the legally protected interests of the investor. If the potentially alternative measure is less disruptive of the legal commitments owed to foreign investors but still equally effective, necessity cannot be invoked. This is probably the hardest condition to assess for an investment tribunal but one that must be verified nonetheless.

[107] In *Thailand-Restrictions on Importation of and Internal Taxes on Cigarettes*, WT/DS10/R, 5 October 1990, para 75, the Panel held that import restrictions may be adopted under Article XX GATT (b) "only if there were no alternative measure consistent with the General Agreement, or less inconsistent with it, which [the concerned State] could reasonably be expected to employ to achieve its health policy objectives".

X. Conclusions

The five decisions by ICSID tribunals on the Argentine necessity pleas present several analogies and differences. The most important difference concerns the co-ordination between Article XI and customary international law as expressed in Draft Article 25 of the Draft Articles on State Responsibility. The priority given to Article XI as *lex specialis* by the *LG&E* and *Continental* Tribunals – in line with the position of the *ad hoc* Committee in *CMS* – is clearly to be preferred. The *Continental* award must further be appreciated insofar as it addressed the necessity plea before determining any *prima facie* violations of the treaty.

The five tribunals unanimously and convincingly held that Article XI is not a self-judging provision. In spite of certain differences as to the relationship between Article XI and Draft Article 25, they also agreed in good substance on the conditions that need to be satisfied in order to invoke Article XI, namely (a) the existence of a crisis serious enough to threaten the economic collapse of the host State; (b) the non-contribution by the host State to the crisis; and (c) the lack of any valid alternative.

These conditions correspond to those existing under customary international law. The major contribution of the *Enron* and *Sempra* awards regards their findings on the interaction between Article XI, customary international law and the general principles of law. From this perspective, customary international law and the general principle of law which prevents a party taking legal advantage of its own fault play an important role in defining the content of Article XI and filling its gaps.

Despite this largely common understanding of the conditions for the adoption of measures on grounds of necessity, the five arbitrations reached remarkably inconsistent conclusions. The risk of inconsistent decisions is inherent in the nature of investment arbitration and cannot but affects the coherence and predictability of the legal protection of foreign investment. However, it is submitted that in the cases under discussion the inconsistent outcomes are essentially due to different assessment of facts rather than disagreement on legal matters.

The most striking feature of all these cases remains the difficulties faced by tribunals in assessing whether these conditions were satisfied. With regard to the specific conditions, it is argued in the first place that the Argentine crisis reached the threshold of gravity which may trigger the adoption of measures on ground of necessity as held in *LG&E* and *Continental*.

The *LG&E* and *Continental* Tribunals seem to be correct also in finding that Argentina did not contribute to the crisis or at least cannot be faulted as it made reasonable efforts to tackle it.

The last condition – lack of alternative measures – has proved particularly problematic, partly because unlike the previous two it requires an investigation on the availability and effectiveness of measures that *could* have been taken instead of an assessment of the situation *existing* at the time of the adoption of the emergency measures, or the conduct of the host State in the period *prior* to the adoption of such measures.

The lack of any alternative is the essence of necessity and must be assessed – as the *Continental* Tribunal did – with regard to the measures adopted as a whole and individually taken. Investment tribunals may also follow the *Continental* Tribunal in borrowing the approach of GATT and WTO adjudicating bodies. Such an approach is based on (a) a process of weighing and balancing of several factors, most importantly the effectiveness of the measures adopted and their impact on the protection of foreign investment, and (b) a comparison between these measures and other potential alternative measures consistent with or less disruptive of the international commitments of the host State.